

Building Owner Survey 2020 (Main Report)

Changes in the environment and business conditions of nationwide small and medium-sized building owners

November 26, 2020

Since 2015, Xymax Real Estate Institute (hereinafter, "Xymax REI") has conducted questionnaire surveys of owners of small and medium-sized buildings nationwide who lease out their buildings (*1), in partnership with the laboratory of Lecturer Kosei Ishida of the Department of Architecture at Waseda University.

In this 5th survey that was conducted between August and September 2020, we continued from the previous survey to ask building owners about the management state of the building lease business, its outlook, and responses to changes in the environment surrounding the buildings through questionnaires and interviews. This report is a summary of the results. This year we also surveyed the impact of the new coronavirus (COVID-19) on the building business and infection control measures, which has already been released in October 2020 (*2).

*1 *Building Owner Survey* from 2015 to 2019: https://www.xymax.co.jp/english/news_research/?type=research
(The surveys from 2015 to 2019 were carried out with the laboratory of Professor Yukio Komatsu.)

*2 *Building Owner Survey (COVID-19 Edition)*, released on October 21, 2020
<https://www.xymax.co.jp/english/research/images/pdf/20201021.pdf>

Key Findings

1. Attributes of building owners

- Age: More than 60% of the business managers were 60 years old or older.
- Number of buildings owned: 60% of the building owners owned one or two buildings; gross floor area (GFA) of main building: 70% of the owners' major buildings had a GFA of less than 1,000 tsubo (1 tsubo=3.3 sqm); building age: 80% of the major buildings were 21 years old or older.

2. Conditions of the building lease business

- With regard to the conditions of the building lease business, the percentage of "Good (will improve)" was 33% for "Over the past year" but dropped significantly to 10% for "Over the next year." The percentage of "Bad (will deteriorate)" rose from 9% to 28%.
- Business DI, which was positive in 2019 and 2020, dropped to a negative range for 2021 (the business condition "Over the next year" in this survey).
- When comparing income and income-related items between "Over the past year" and "Over the next year," all items except for vacancies saw an increase of a "decreasing" trend by more than 10 points. The percentage of "Decreasing" significantly outweighed that of "Increasing."
- As for expenditure (expenses) and expenditure-related items, the "increasing" trend outweighed the "decreasing" trend in all items except for utility costs. In particular, more than 50% of the operators replied that repair costs were increasing.

3. The building lease business going forward

- For both short-term (around 3 years) and medium- to long-term (5–10 years), the percentage of pessimistic views (sum of "Pessimistic" and "Somewhat pessimistic") significantly outweighed that of optimistic views (sum of "Optimistic" and "Somewhat optimistic"). Compared to the short-term outlook in 2019, optimistic views dropped from 34% to 15%, indicating uncertainties in the short-term outlook due to COVID-19.

- As for future changes in social conditions, building owners' interest was high in "Changes in places to work (spread of telework)," "Infection (COVID-19) control measures," "Decreases in population and workers," and "Changes in work styles (work hours, form of employment)," in this order. Interest in "Changes in places to the work" and "Changes in work styles" was significantly higher than in 2019.
- Measures to improve the value of buildings that were implemented the most were "Energy-saving of equipment," "Refurbishment of common area interior," and "Ensuring seismic performance," in this order.

4. Thoughts on the building lease business going forward

- We introduce some of the building owners' thoughts on the business going forward.

1. Attributes of Building Owners

Building lease business operators

More than 60% of the managers of the building lease business were 60 years old or older (**Figure 1**). The experience of the managers was equally spread (around 20%) among “up to 30 years,” “up to 40 years,” and “up to 50 years” (**Figure 2**). The attributes of building owners were roughly the same as in previous surveys.

Figure 1: Age of Managers (n=940)

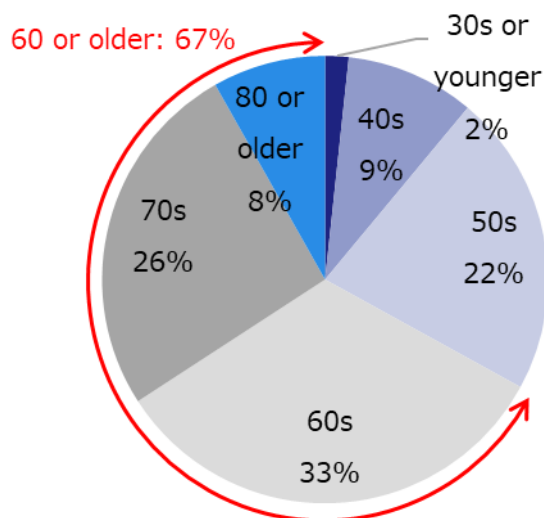
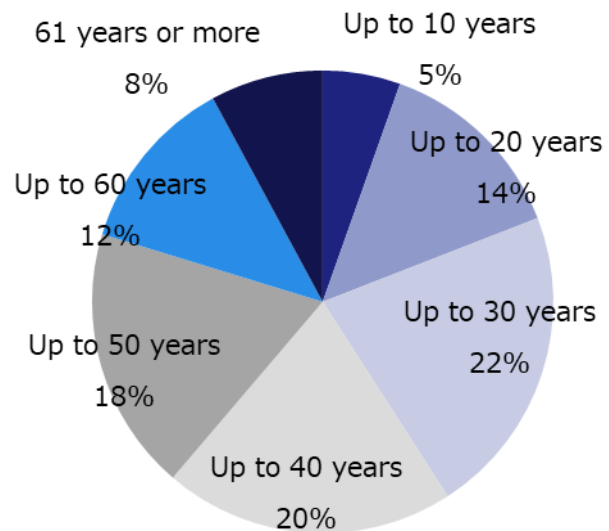
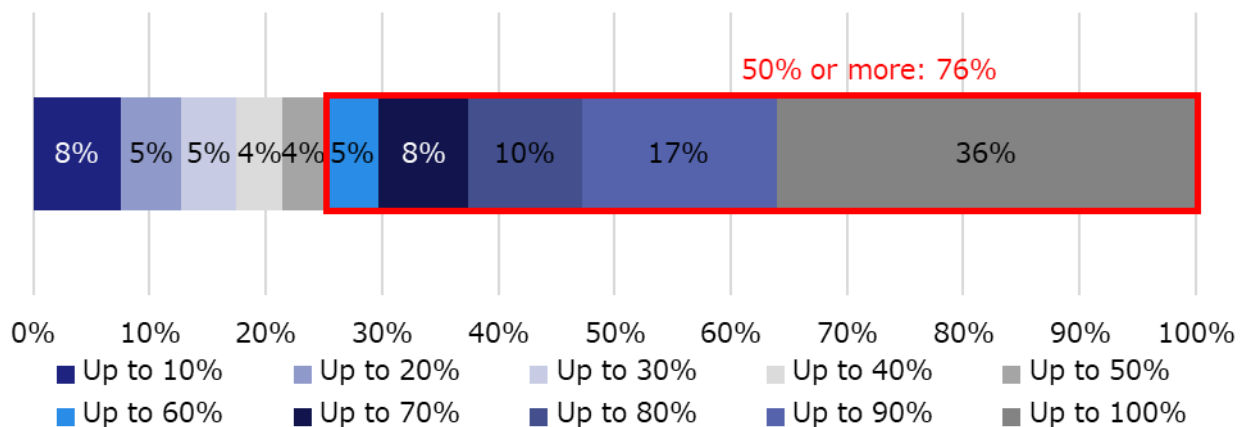


Figure 2: Experience in Building Lease Business (n=937)



Sales of the building lease business accounted for 50% or more of total sales by more than 70% of all respondents, indicating that many respondents were pure-play building lease operators (**Figure 3**).

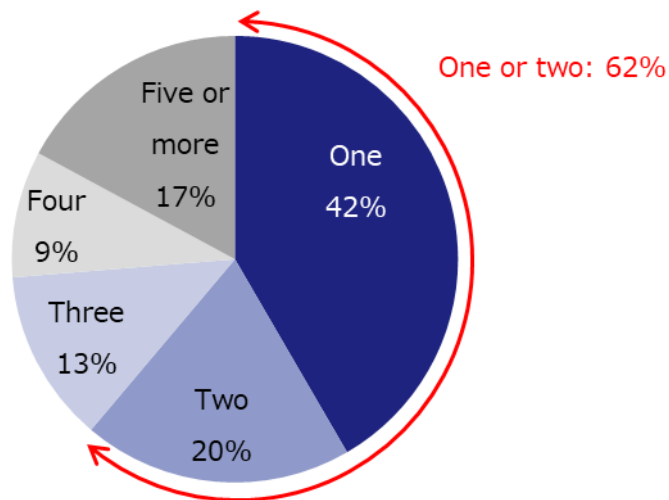
Figure 3: Building Lease Business's Share of Total Shares (n=932)



Buildings owned

Around 60% of all respondents owned one or two buildings in total, while 17% of total owned five or more (Figure 4).

Figure 4: Total Number of Buildings Owned (n=829)



We asked the respondents the size (GFA) and age of the main building in their portfolio. In terms of size, around 70% were less than 1,000 tsubo (Figure 5). As for the completion year, around 80% of the buildings were completed in or before the 1990s (aged 21 years or older) (Figure 6).

Figure 5: Size of Main Building (n=826)

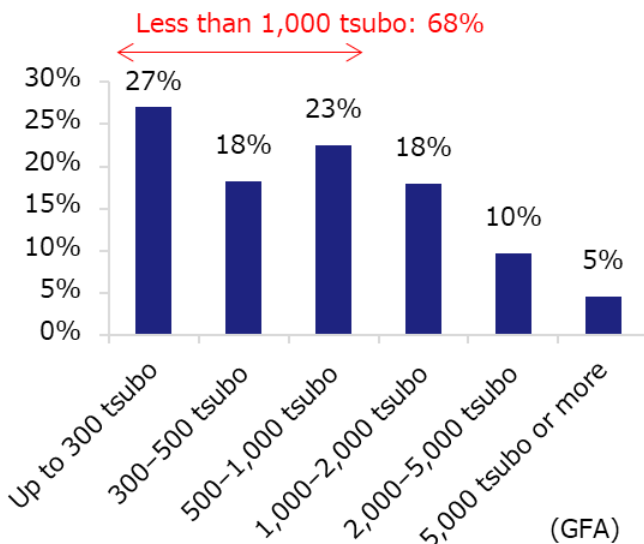
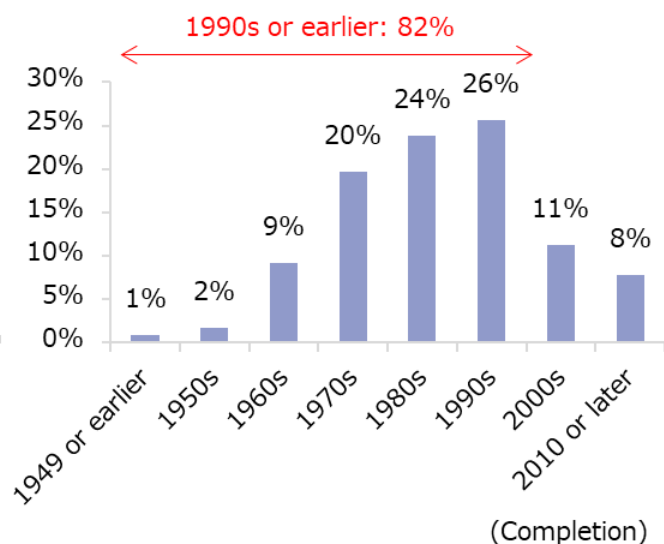


Figure 6: Completion Year of Main Building (n=848)



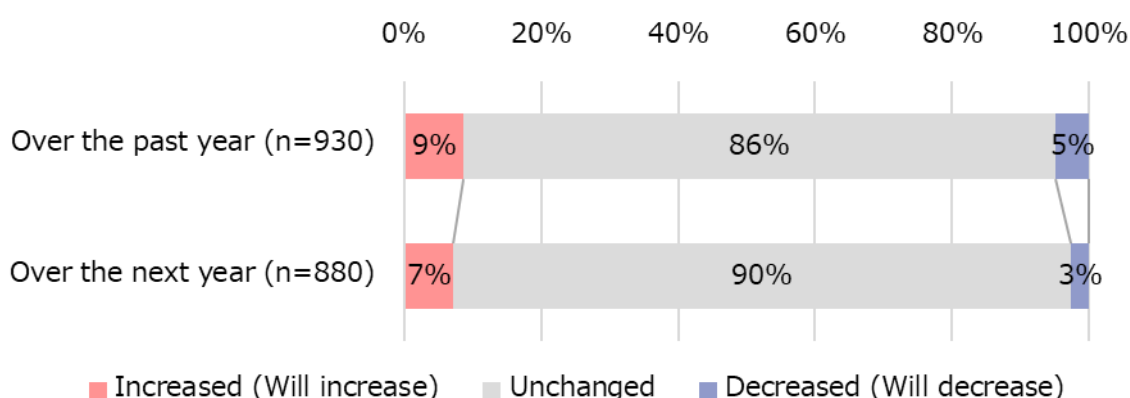
2. Conditions of the Building Lease Business

We asked the operators about the overall conditions of the building lease business “over the past year” and “over the next year.”

Situations of buildings owned

Around 10% of the respondents replied that the number of buildings they owned “increased (will increase)” both “over the past year” and “over the next year,” outweighing those whose number of buildings “decreased (will decrease)” (**Figure 7**).

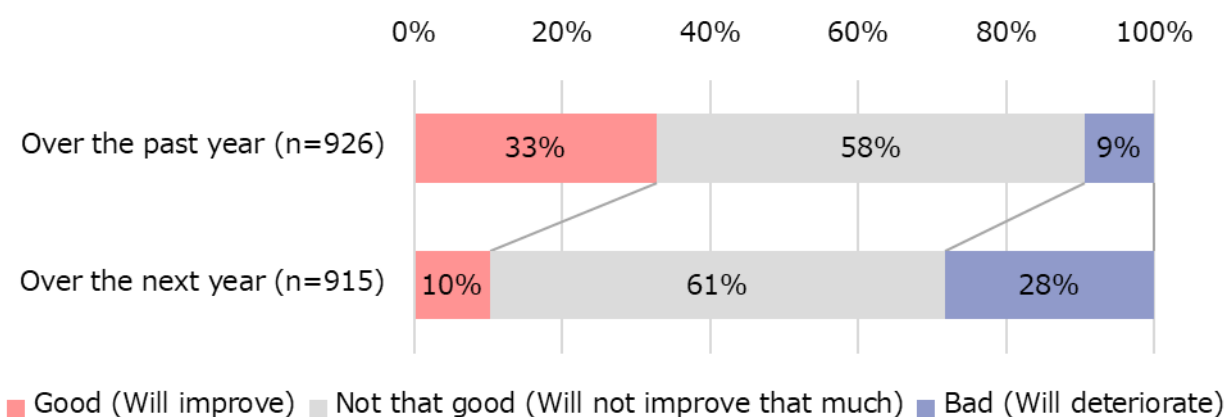
Figure 7: Number of Buildings Owned

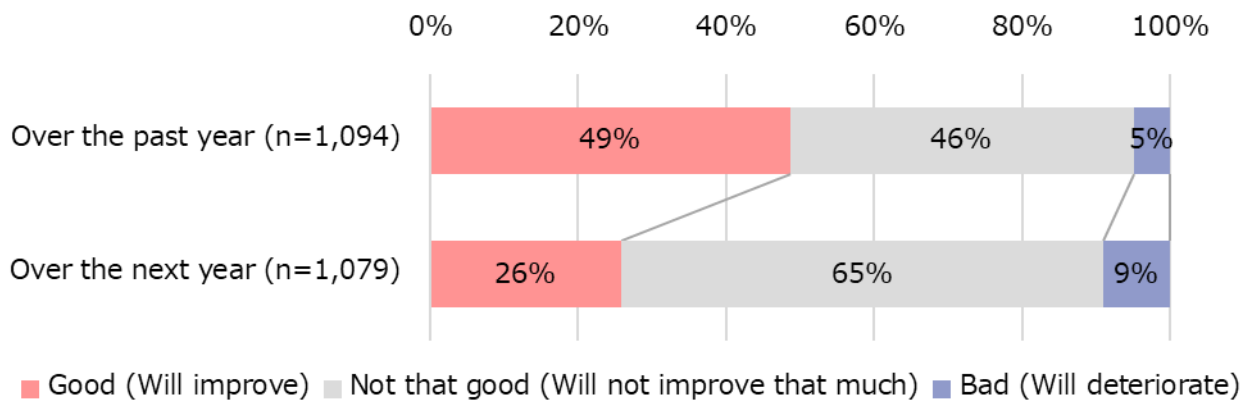


Conditions of the building lease business

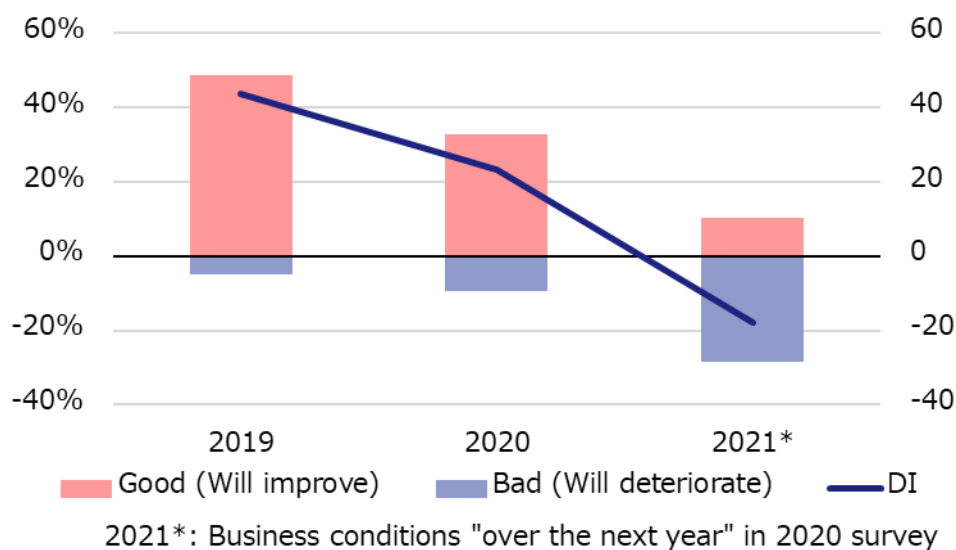
As for the conditions of the building lease business, the percentage of respondents who replied that business conditions were “good (will improve)” dropped significantly from 33% for “Over the past year” to 10% for “Over the next year” (**Figure 8**). Meanwhile, “Bad (will deteriorate)” increased from 9% to 28%. When we compare the “Good (will improve)” and “Bad (will deteriorate)” replies for “Over the next year” with the 2019 survey (**Reference 1**), “Good (will improve)” outweighed “Bad (will deteriorate)” in 2019, while “Bad (will deteriorate)” outweighed “Good (will improve)” in the 2020 survey. Interviews with building owners revealed operators’ concerns about the outlook of the business, including anxieties toward tenants moving out or reducing occupying area and drops in rent due to the prolonged pandemic, the spread of telework and changes in work styles.

Figure 8: Conditions of the Building Lease Business



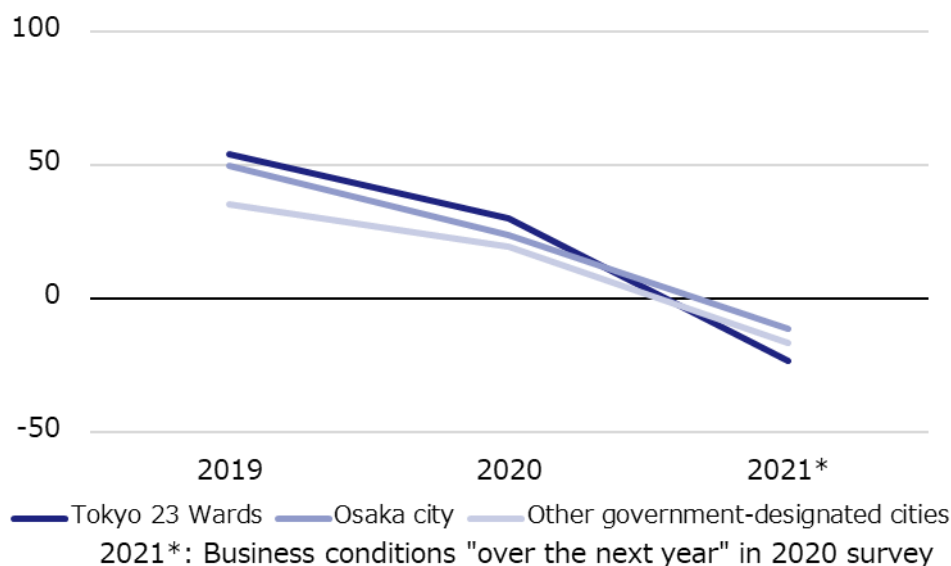
Reference 1: (2019 Survey) Conditions of the Building Lease Business

We then examined the changes over time in business conditions in terms of DI—the percentage of "Good (will improve)" minus that of "Bad (will deteriorate)" (**Figure 9**). A figure larger than zero means that many operators replied "Good (will improve)," while a figure less than zero means that many operators replied "Bad (will deteriorate)." The DI was in the positive range in 2019 and 2020, which means that the percentage of "Good" was large, but dropped to a negative in 2021 ("Over the next year" in this survey), indicating that many operators expected business to deteriorate.

Figure 9: Business Conditions DI

We also examined the change of DI over time for Tokyo 23 Wards, Osaka city and other government-designated cities. As in the overall DI, the DI dropped in all areas between 2019 and 2021. In particular, the 2021 DI in Tokyo 23 Wards and Osaka dropped more sharply than in other government-designated cities (**Figure 10**).

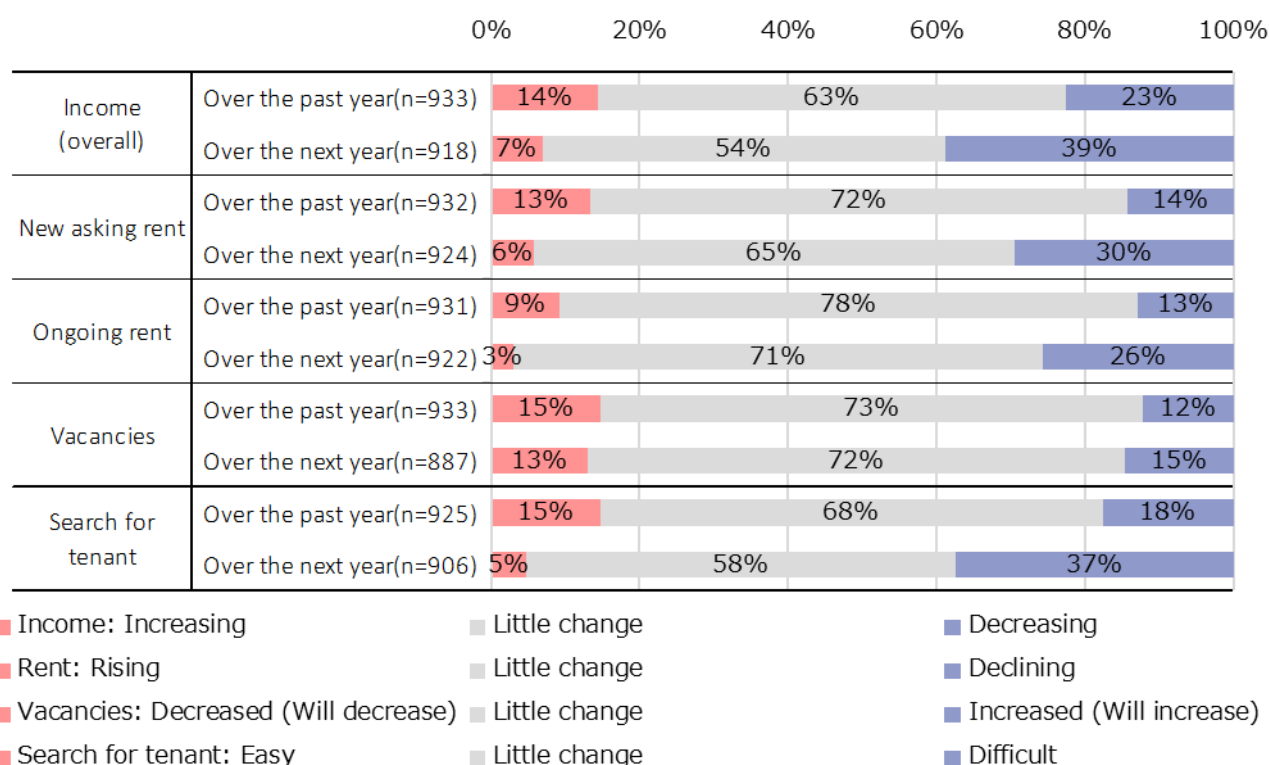
Figure 10: Business Conditions DI (By Area)



Income of the building lease business

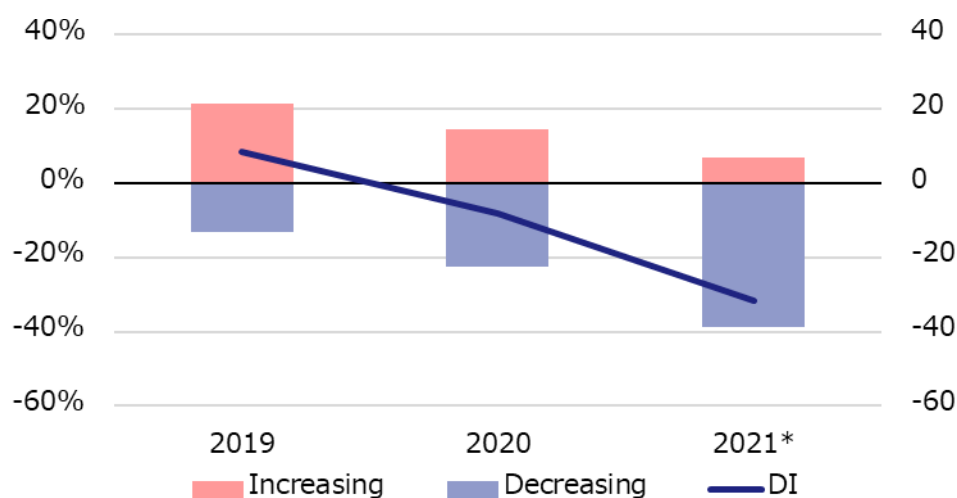
We compared the items related to building lease business income between "Over the past year" and "Over the next year" (**Figure 11**). "Decreasing" rose by more than 10 points in items other than vacancies and significantly outweighed "Increasing."

Figure 11: Income of the Building Lease Business



We then calculated the DI for income (overall) by subtracting "Decreasing" from "Increasing" (**Figure 12**). The DI was plus in 2019 but dropped to a minus in 2020 and is expected to deteriorate in 2021 by many operators.

Figure 12: DI of Income (Overall)



2021*: Business conditions "over the next year" in 2020 survey

Expenditure (expenses) of the building lease business

For expenditure (expenses) of the building lease business, many operators replied most of the items were "Increasing" both "Over the past year" and "Over the next year," outweighing "Decreasing" (**Figure 13**). In particular, repair costs saw the largest percentage of "Increasing," which was more than 50%. Only utility costs had more operators replying "Decreasing" than "Increasing," and had a larger percentage of "Decreasing" than other items. According to the interview results, the main factor was the replacement of equipment to energy-saving LEDs, air conditioners, etc. when tenants moved out.

Figure 13: Expenditure (Expenses) of the Building Lease Business

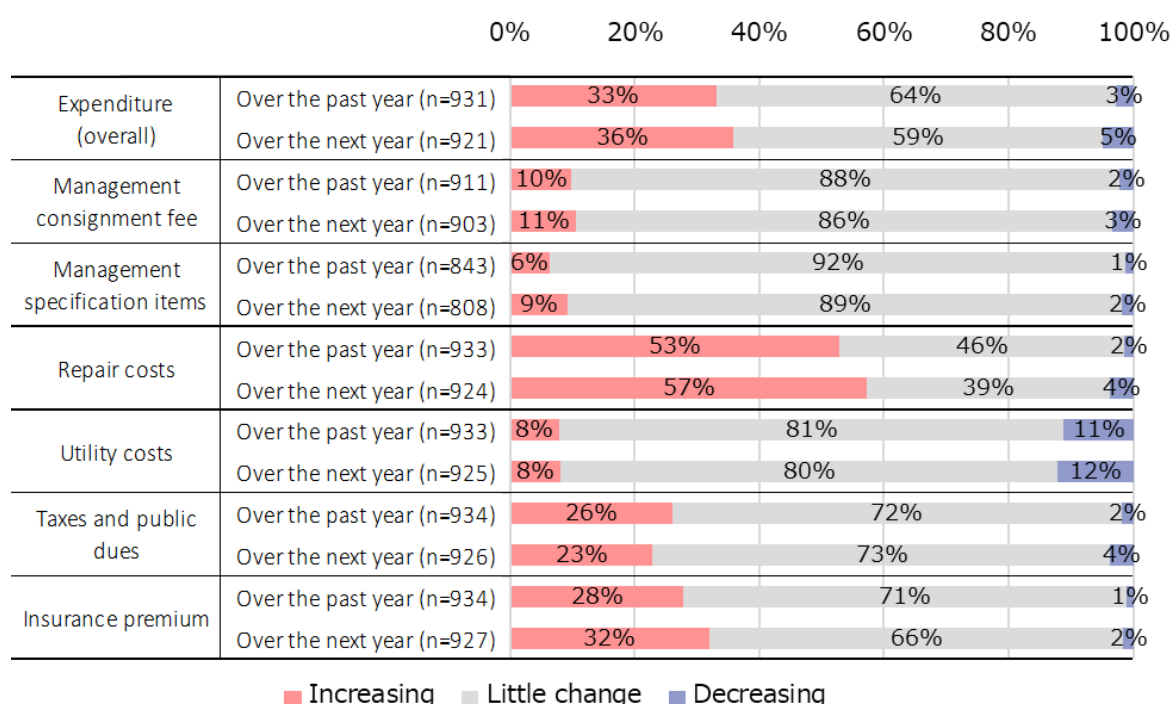
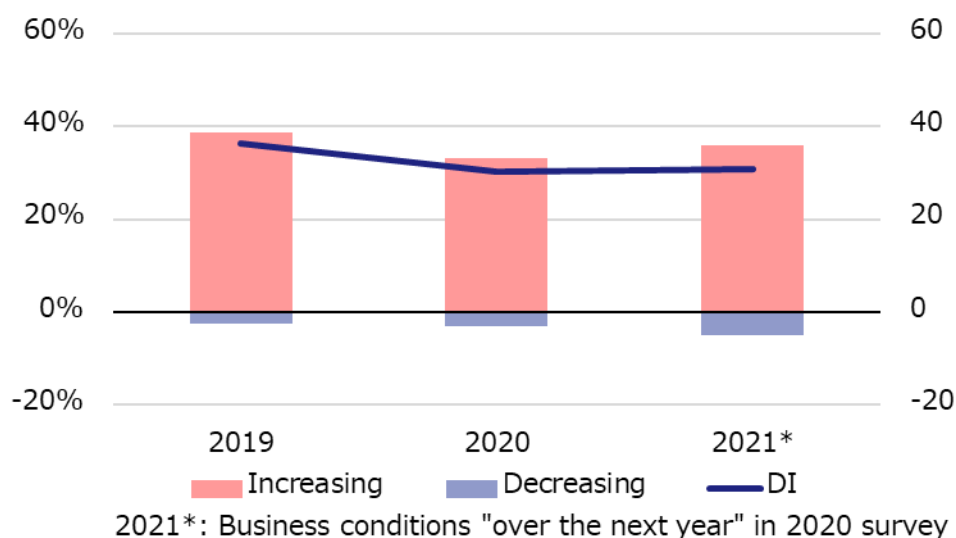


Figure 14 shows the expenditure trend in terms of DI, as in income. There are no significant differences after 2019. Expenditure is continually on a rising trend.

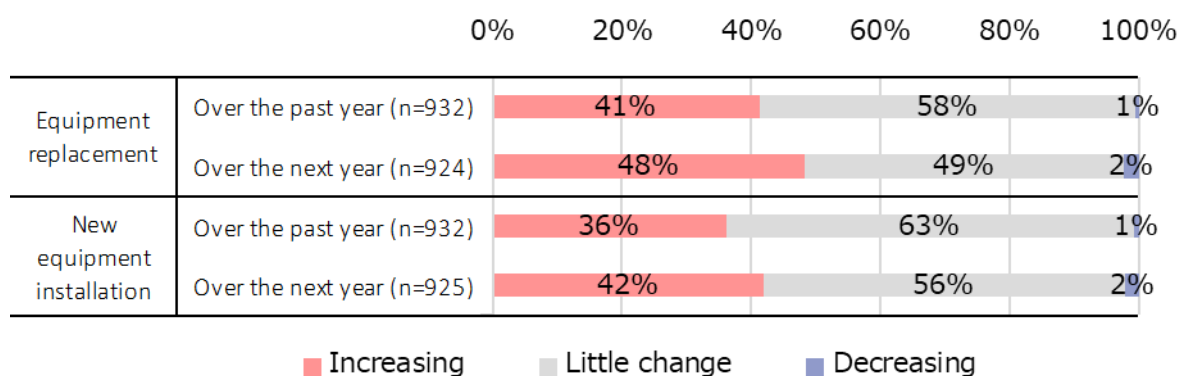
Figure 14: DI of Expenditure (Overall)



Capital expenditure of the building lease business

Capital expenditure that accompanies replacement and new installation of equipment was increasing, as in expenditure (expenses) (**Figure 15**). The rising trend of expenditure seems to be continuing due to replacement and revamping of large equipment, in addition to repairs.

Figure 15: Capital Expenditure of the Building Lease Business

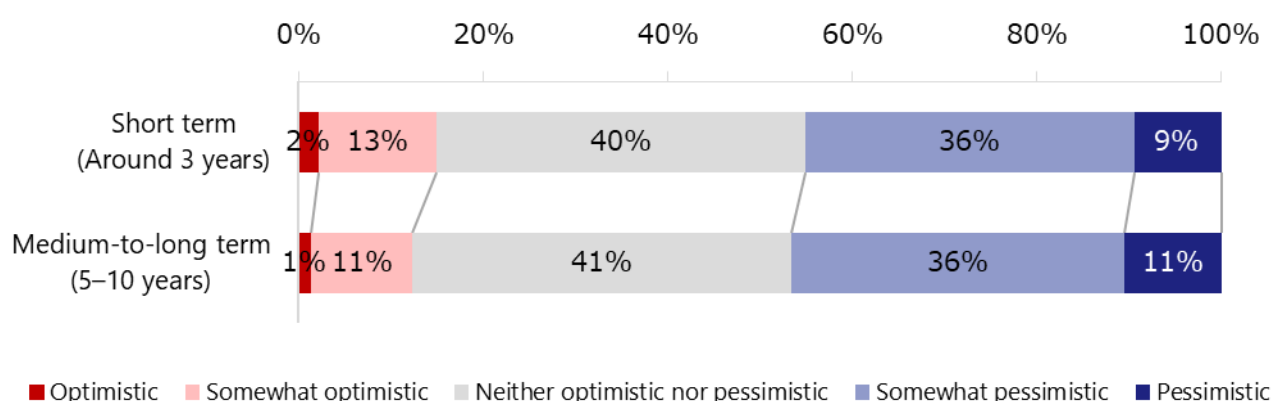


3. The Building Lease Business Going Forward

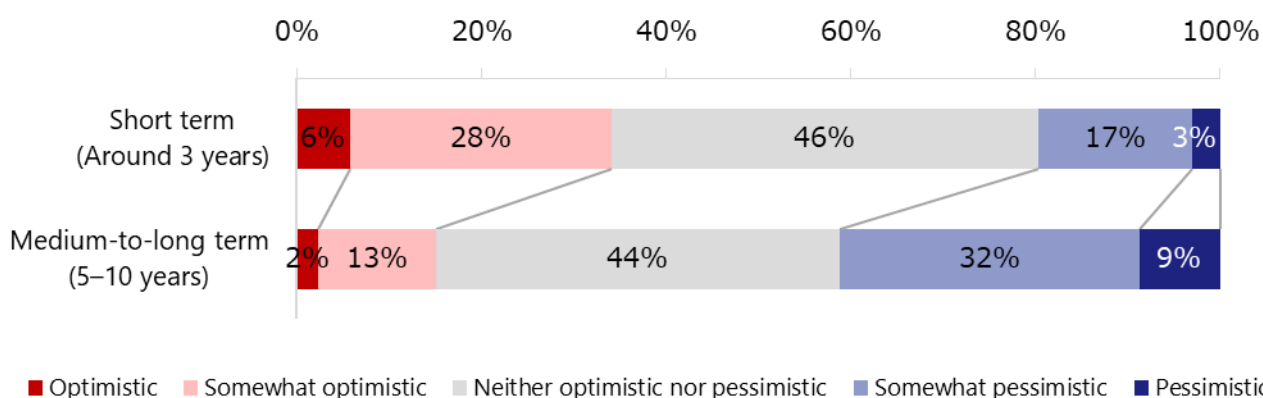
Outlook

As for the outlook of the building lease business, pessimistic views (the sum of “Pessimistic” and “Somewhat pessimistic”) significantly outweighed optimistic views (the sum of “Optimistic” and “Somewhat optimistic”) both in the short term (around 3 years) and the medium- to long term (5–10 years) (**Figure 16**). While the medium- to long-term outlook was similar to the 2019 survey, the short-term outlook saw a drop in optimistic views from 35% in 2019 to 15% in 2020 (**Reference 2**). More operators may have become pessimistic in 2020, which has been hit by a pandemic, due to uncertainties in the outlook not only in the medium- to long term but also in the short term.

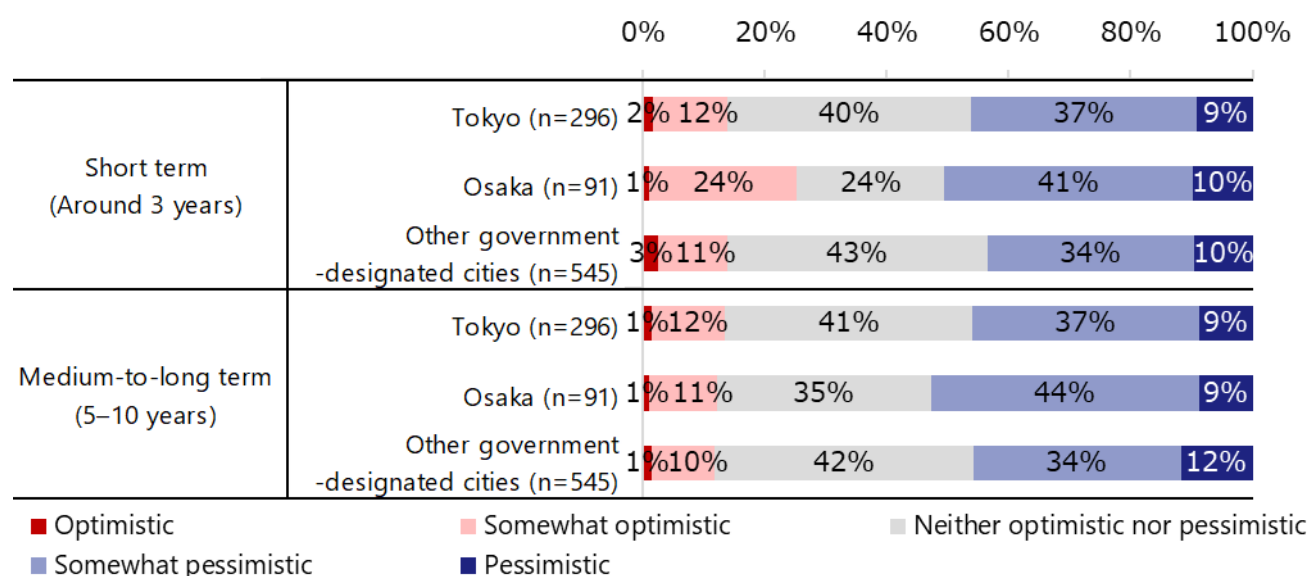
Figure 16: Outlook (Short-term: n=925; Medium- to Long-term: n=925)



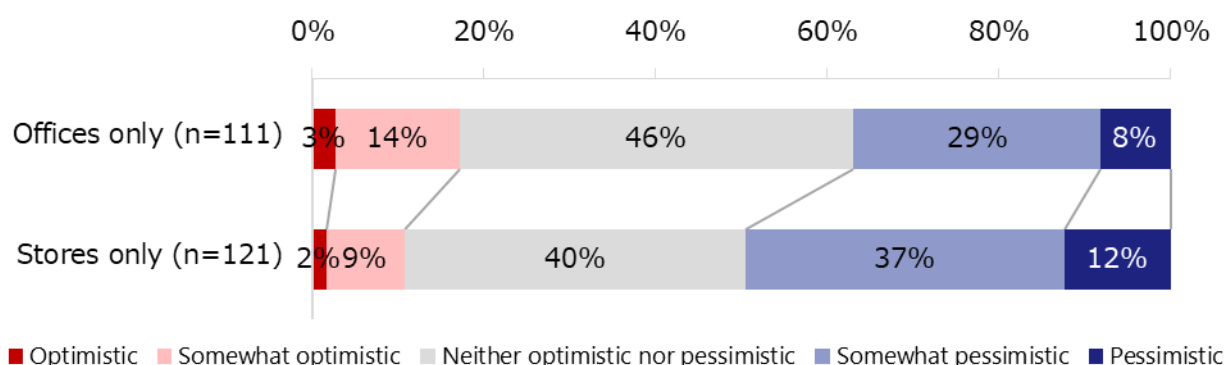
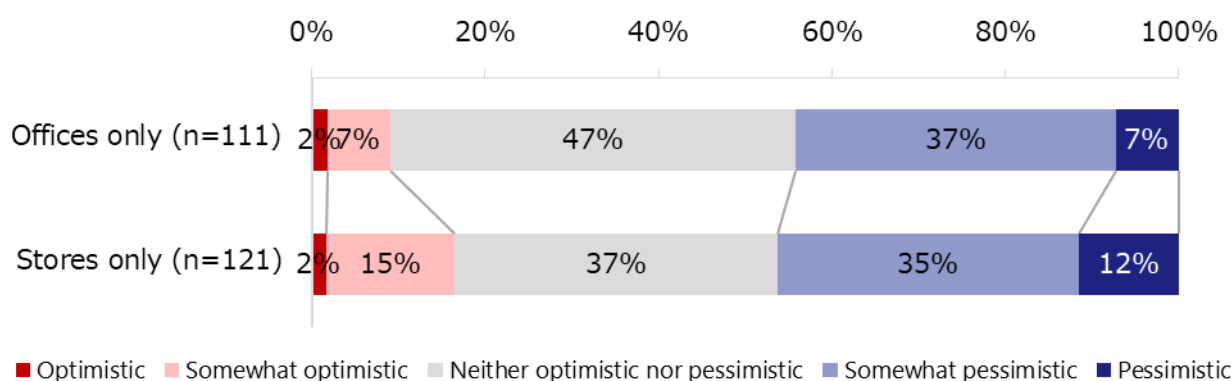
Reference 2: (2019) Outlook (Short-term: n=1,106; Medium- to Long-term: n=1,106)



We compared building owners’ outlook of the business by grouping them into the area where their buildings are located: Tokyo 23 Wards, Osaka city, and other government-designated cities (**Figure 17**). There was no significant difference between Tokyo 23 Wards and other government-designated cities, but Osaka showed larger percentages of optimistic views over the short term and of pessimistic views over both the short term and the medium- to long term than other areas. According to the interviews, while there was some source for optimism such as a shortage of office supply due to the rebuilding of office buildings into hotels and condominiums as well as expectations toward a recovery of demand from overseas visitors to Japan after the pandemic has abated, building owners were concerned about the scheduled large supply of properties and the previous supply balance of hotels and condominiums.

Figure 17: Outlook (By Area)

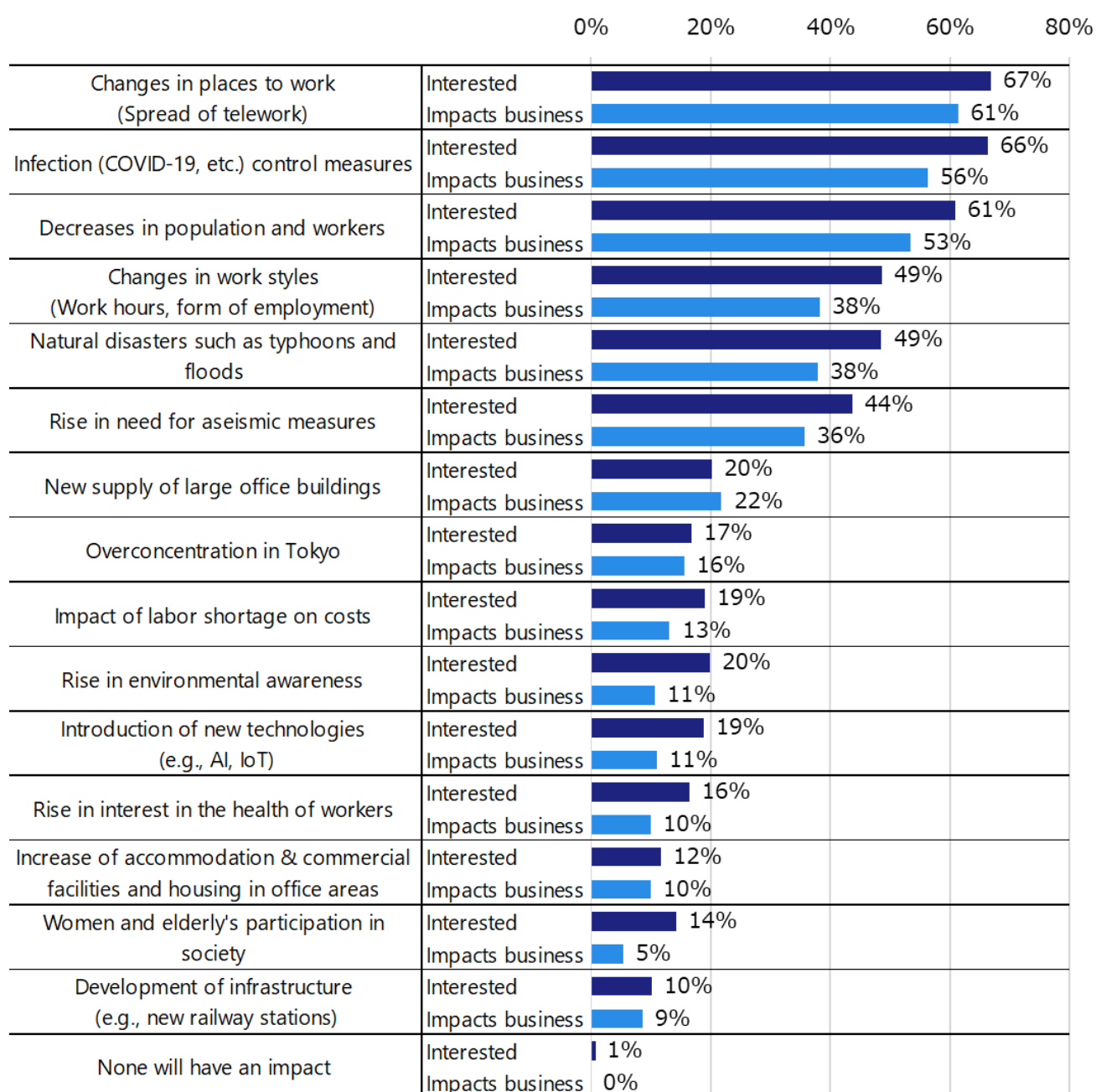
We also examined the difference in outlook by tenant type by grouping the operators into those with office tenants only and those with store tenants only (**Figure 18**). In the short-term outlook, operators with office tenants only were more optimistic and less pessimistic than operators with store tenants only. In the medium-to long-term outlook, operators with store tenants only were more optimistic than those with office tenants.

Figure 18: Outlook (By Tenant Type)**Short-term outlook****Medium- to long-term outlook**

Interest in future changes in social conditions and impact on own business

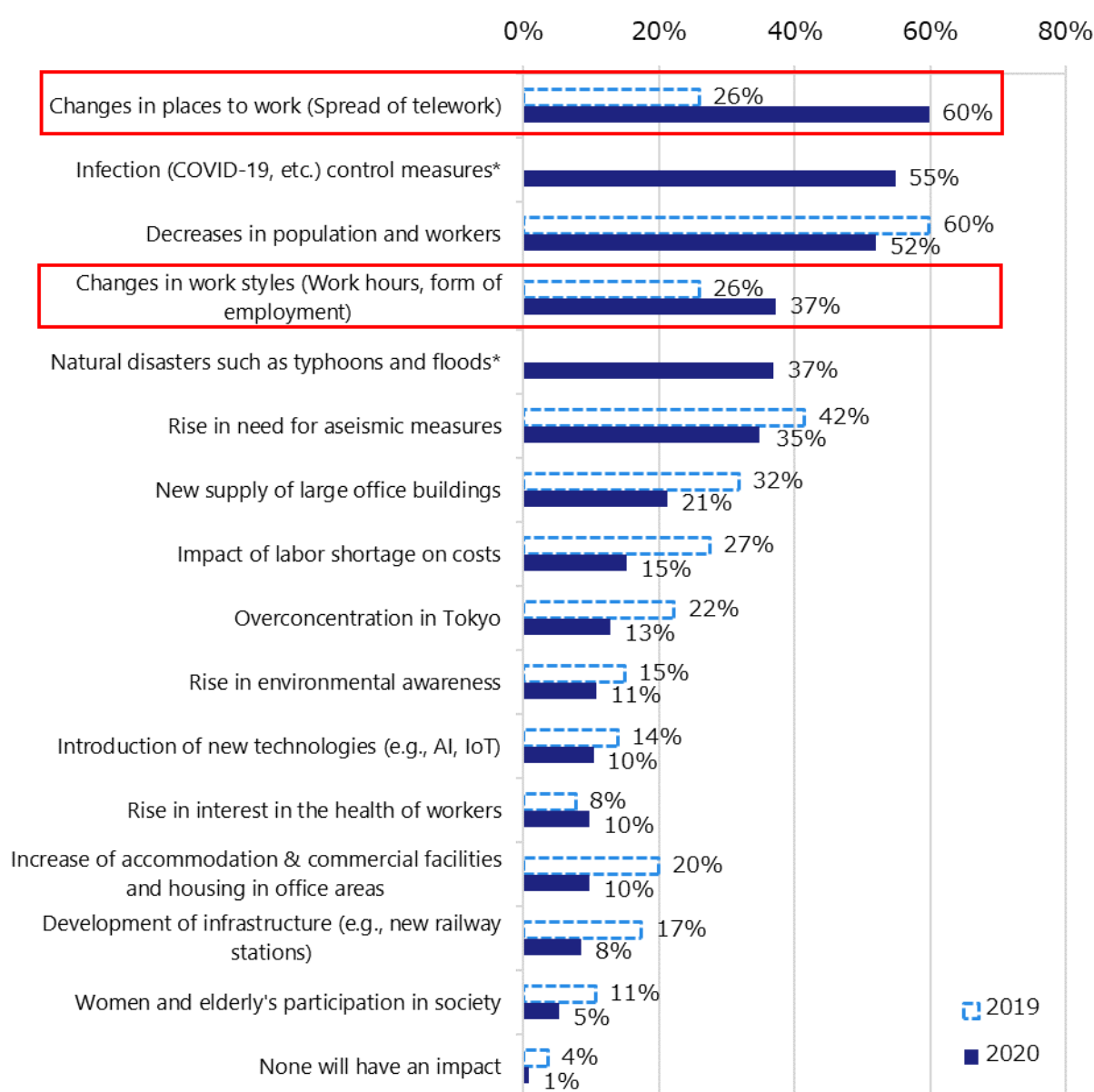
We asked the operators about their interest in future changes in social conditions and the impact on their business (**Figure 19**). The top choice in terms of interest and impact on own business was "Changes in places to work (spread of telework)." This was followed by "Infection (COVID-19) control measures," "Decreases in population and workers," and "Changes in work styles (work hours, form of employment)."

Figure 19: Future Social Condition Changes Interested in and Impact on Own Business
(Changes Interested in: n=929; Impact on Own Business: n=921)



We then compared the changes in social conditions that may affect the operators' building lease business with the result of the 2019 survey (**Figure 20**). The percentages were smaller in 2020 than in 2019 in general, except for "Changes in places to work (spread of telework)" and "Changes in work styles (work hours, form of employment)," which increased between 2019 and 2020. In particular, the percentage of "Changes in places to work (spread of telework)" more than doubled. In the interviews, many operators expected the spread of telework to have a major impact on the building lease business going forward. Some also said that it was difficult to determine whether telework would continue after the pandemic and whether they would need to make adjustments to the equipment and layout of the buildings.

Figure 20: Changes in Social Conditions that May Affect Own Business in Future (2019 vs 2020)
(2019: n=1,106; 2020: n=946)

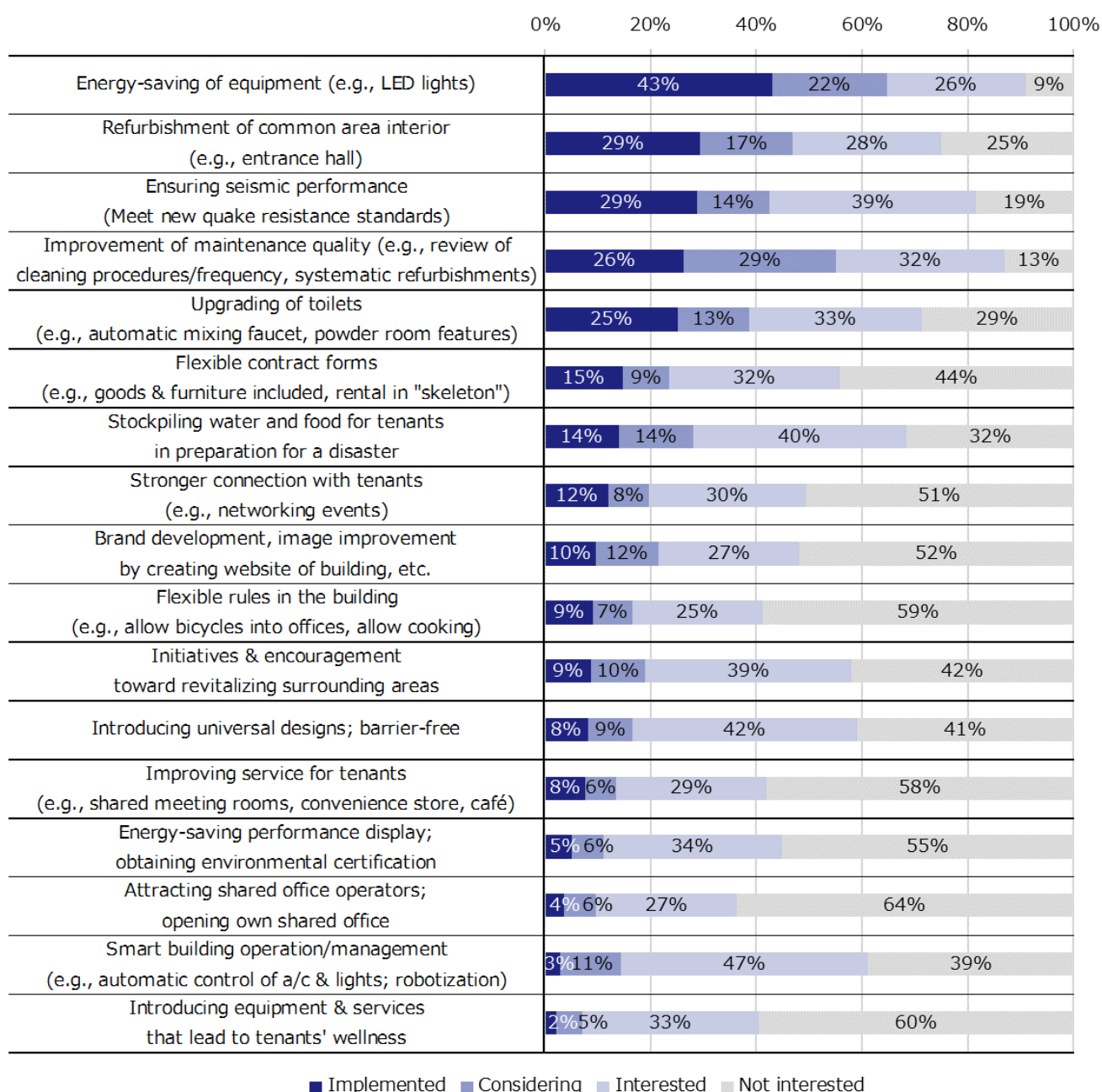


*Option did not exist in 2019 survey

Measures to improve the value of buildings

We asked the operators about their implementation of measures to improve the value of buildings (**Figure 21**). The measure that was implemented the most was “Energy-saving of equipment (e.g., LED lights)” (43%), followed by “Refurbishment of common area interior (e.g., entrance hall)” (29%) and “Ensuring seismic performance (meet new quake resistance standards)” (29%). The results were roughly the same as in previous surveys.

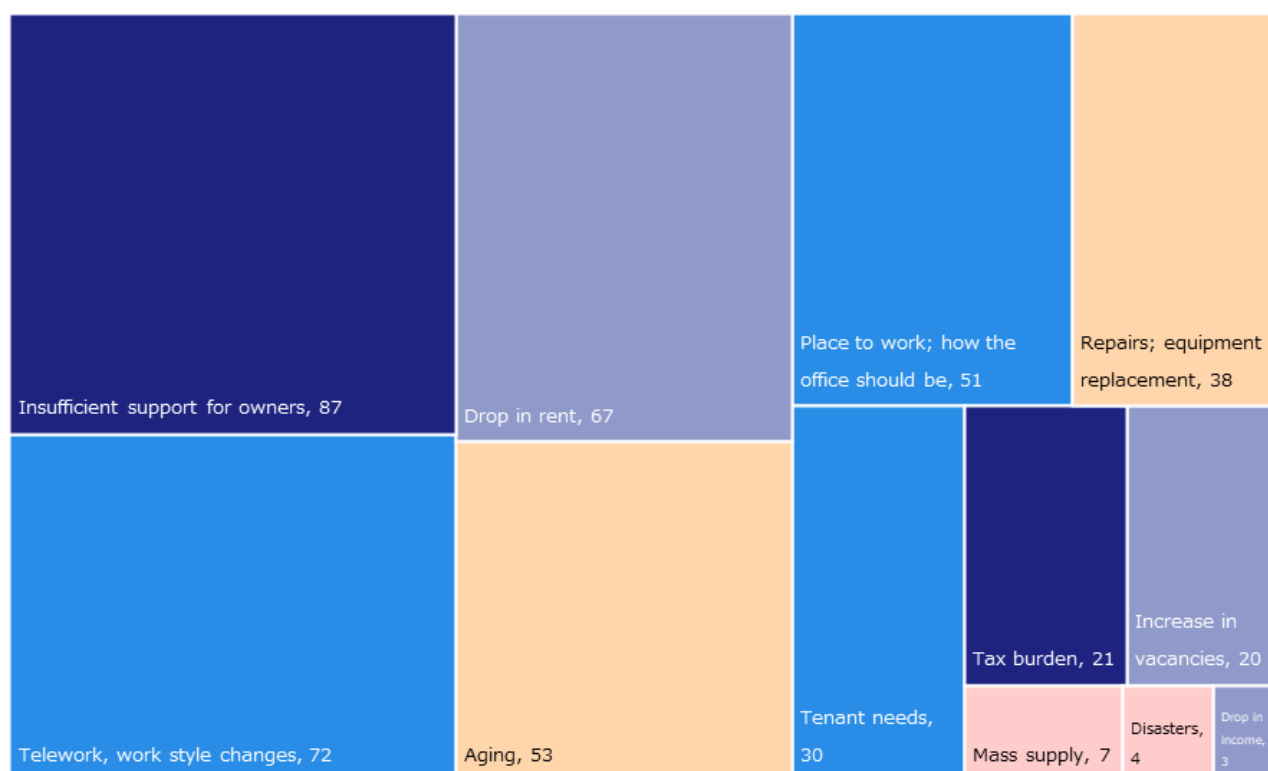
Figure 21: Measures to Improve the Value of Buildings and Implementation Status (n=926)



4. Thoughts on the Building Lease Business Going Forward

We asked operators about their concerns toward the building lease business going forward in view of changes in social and surrounding environments (write-in answers). We extracted the words that frequently appeared in the answers and sorted them in **Figure 22**. The sizes of the squares are proportionate to the number of building owners who showed an interest in the matter.

Figure 22: Concerns in the Building Lease Business Going Forward (Frequently Appearing Words)



Impact of COVID-19: ■ Burden on the owner; ■ Changes in work styles, how the office should be; ■ Management (drop in income)
Buildings and others: ■ Buildings; ■ Other environmental changes

Comments on the impact of COVID-19 were especially numerous in the main survey of 2020. As owners face concerns in income amid requests by tenants to reduce the rent or tenants moving out, many of them mentioned that support for building owners was insufficient. In addition to concerns toward a drop in rent and an increase in vacancies due to the prolonged pandemic, they also face challenges in how they should change the layout of their buildings in the future or the equipment they will introduce, following the changes in the places to work due to the spread of telework. On top of their anxieties toward a stable income, they also expected costs to increase, such as for renovations and repairs due to the aging of their buildings, measures against natural disasters such as earthquakes and floods, and infection control measures.

In the following pages we introduce some of the voices of building owners obtained from the interviews and comments in the questionnaire.

Impact of COVID-19 on business

- I have a feeling that tenants will be more inclined to relocate from a large building to a small/medium building.
- I am concerned about tenants' reductions of rentable area and relocations to another building due to the effect of telework, etc.
- I am worried that work patterns would change drastically and lead to a fall in demand for buildings due to the spread of telework, etc.
- Since our main tenant is an IT-related distributor, I am worried that they may reduce the rentable office area due to an increase in telework and sales activities without dropping in at the office.
- I am concerned that vacancy periods might be prolonged, or contract rent might decline, unlike in the past.
- I am anxious about whether the restaurants in the building I rent out, which is located in a nearby office district, can remain in business going forward.
- I despair by the thought of cancellations that might occur due to the prolonged pandemic, since most of my tenants are restaurants.
- My primary business is renting out a business hotel. Users from abroad accounted for an increasing share of non-business users up until last year. Since business use of the hotel might also decrease due to telework, etc. going forward, I am worried that my tenant will continue to rent the building as a hotel.

The outlook of buildings going forward

- The offices may change drastically in the future as telework spreads further due to COVID-19. I intend to keep a close eye on how the ideal form of office buildings will change.
- I can no longer continue doing business with the previous types of tenants. When I advertise for new tenants next time, I will have to carefully consider the industry of the tenant and their purpose of using the building.
- I might have to offer new contract methods and usages of offices, such as weekly contracts.
- With an increase in vacancies expected in the future, it might become difficult to wish for companies to rent my building as their office. It is a problem for me since my building is not designed for rental offices or shared offices. I am very concerned about how to survive.
- There has been an increase in usage as a rental meeting room (for remote meetings). This is probably because the users don't have a closed meeting room in their room. The usage and layout of offices might change in the future.
- I expect telework to become common and established as a work style even after the pandemic has abated. I am considering offering new residences (rental) that can accommodate telework.
- It is hard to discern how much capital expenditure should be made to control COVID-19 infection, amid uncertainties as to when the pandemic will end. It is difficult to determine whether that expenditure should simply be made to improve the quality of the building.
- I am interested in whether a new office building operation system will emerge from changes in work patterns.
- I feel that we must think of new ways to build buildings since natural disasters have been increasing in scale recently. Since the population is also shrinking, I believe that we must streamline business management, such as by reducing construction costs and being able to rebuild buildings immediately after a disaster hits.

Measures against natural disasters (including COVID-19)

- We will be required to operate buildings that include equipment anticipating various disasters, such as earthquakes, typhoons, floods, and infectious diseases.
- I had stockpiled emergency rations and water for the full capacity of each tenant, but face masks and alcohol disinfectants were far from enough.
- The air conditioners do not function without some interior air recirculation. I must think of a way for air conditioning to be fully functional by only taking in outside air.
- The Kumamoto floods caused an overcapacity of underground drainage and backflow of drainage due to the deterioration of water supply and sewage piping in Kumamoto city. Since old buildings with underground floors all suffered from water leakage, we must combat the great challenge of natural disasters before we start talking about COVID-19.

Aging of buildings and equipment

- As both the building frame and equipment are aging, I am concerned about the rise in maintenance costs going forward.
- My worry is about rebuilding the building due to aging amid a drop in rent income from the pandemic.
- I am also considering selling the building since repair costs have increased due to the aging of the building.
- Revamping and repair costs for equipment have risen due to the aging of the building. Buildings are living things—they can only be utilized if they are managed and maintained.
- I want to rebuild the building or carry out a major repair since it is now 30 years old, but my cash flow situation is very precarious.
- I was thinking of rebuilding the aged building but am now also considering renovating it since the outlook of the social situation has become uncertain due to COVID-19.

Others

- Buildings are becoming oversupplied, and I am thinking that I must consider rebuilding my building at the right moment to maintain competitiveness.
- I am concerned about the damage to the supply-demand balance due to the continued new supply of large buildings in my area.
- I face many cases where I am demanded huge compensations for eviction upon rebuilding the building from tenants whose contracts are old and are not fixed-term tenancies. I wish the Act on Land and Building Leases will be amended to reflect the reality of the business.

Summary

Xymax REI has been examining the situation of building owners since 2015 and has revealed the conditions of the building lease business, the outlook of the business, and building owners' awareness of changes in social conditions. Many of the owners of small and medium-sized buildings are elderly and own only one or two buildings, the majority of which are aged more than 20 years. We have found that they were concerned about their medium- to long-term outlook due to the possible increase in expenditure, such as repair costs for old buildings and property taxes.

The previous surveys had revealed that building owners were interested in the impact of the population decline, natural disasters, and environmental changes to surrounding areas on the building lease business. In this 5th survey, we found that building owners were more interested in the prevention of COVID-19 infection and changes in tenants' values and needs. Going forward, building owners will have to make various efforts and initiatives both in the tangible and intangible aspects of their buildings, while assessing the rental office market and changes in tenant needs. Such initiatives by building owners will not only enable them to maintain and improve the competitiveness of their buildings but will also become the foundation for developing quality stock.

Xymax REI intends to continue surveys of building owners and gather best practices (*3) on a regular basis to offer beneficial information.

*3 *Best Practices of Small-to-Medium-Sized Buildings –The 2nd Report*, released on April 7, 2020
<https://www.xymax.co.jp/english/research/images/pdf/20200407.pdf>

Survey Overview

Period	August – September 2020
Coverage	<p>21 government-designated cities (Sapporo, Sendai, Tokyo 23 Wards, Saitama, Chiba, Yokohama, Kawasaki, Sagami-hara, Niigata, Shizuoka, Hamamatsu, Nagoya, Kyoto, Osaka, Sakai, Kobe, Okayama, Hiroshima, Kitakyushu, Fukuoka, Kumamoto)</p> <p>A total of 10,830 companies extracted from Tokyo Shoko Research (TSR)'s data</p> <p>[Net sales] 10 million–3,000 million yen (30 million–3,000 million yen for Tokyo)</p> <p>[Industry] Companies whose “principal” or “secondary” business (thus registered) is office lease</p>
Number of valid answers	<p>Questionnaire: 946 companies; 8.7% response rate</p> <p>(Number of companies: 63 in Sapporo, 57 in Sendai, 298 in Tokyo 23 Wards, 25 in Saitama, 9 in Chiba, 66 in Yokohama, 28 in Kawasaki, 4 in Sagami-hara, 7 in Niigata, 13 in Shizuoka, 7 in Hamamatsu, 65 in Nagoya, 41 in Kyoto, 92 in Osaka, 9 in Sakai, 32 in Kobe, 15 in Okayama, 34 in Hiroshima, 20 in Kitakyushu, 44 in Fukuoka, 17 in Kumamoto)</p>
Method	Questionnaire survey by post or online and interview
Topics	<p>I. About the respondent company Age of manager; business experience; share of sales of lease business; number, age, area of buildings owned, etc.</p> <p>II. Situation of the office building lease business Situation of buildings owned; business condition; income; expenditure, etc.</p> <p>III. Office building lease business going forward Outlook (short-term, medium- to long-term); social conditions interested in; social conditions affecting the building lease business; measures to improve the value of buildings, etc.</p> <p>IV. Impact of COVID-19 on the company Events that occurred in managing rental buildings; Infection control measures</p>

*The figures indicated in the charts contained in this report are rounded to the first decimal place and therefore may not add up to 100%.

*The charts contained in this report exclude non-responses.

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